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No. 83-1430

IN THE

Supreme Court of the United States

OCTOBER TERM, 1983

J. BARANELLO & SONS,

Plaintiff-Petitioner,

— against —

CITY OF PATERSON,

Defendant-Respondent.

ON WRIT OF CERTIORARI TO THE SUPREME COURT OF NEW JERSEY

PETITIONER'S REPLY BRIEF ON PETITION FOR CERTIORARI

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ARGUMENT

Points Raised by Respondent

This Reply Brief is respectfully submitted on behalf of petitioner J. Baranello & Sons ("Baranello") in response to the Brief in Opposition of respondent City of Paterson ("the City"). The City argues at Point I that Baranello cannot enforce the arbitration award because the federal statute was not raised at the state court level, and at Point II that the arbitration award should not be allowed to stand because the arbitrators may have awarded damages based upon a misinterpretation of the contract. The City fails to cite a single decision under the federal Arbitration Act in support of its position that the award should be vacated, and purports to rely instead upon "the well settled principle that courts will not permit arbitrators to ignore contract provisions", and upon precedents from the New Jersey courts, which have frequently overturned arbitration awards in recent years and appear to have adopted the view that the federal Arbitration Act need not be applied by state courts.

This Reply Brief will demonstrate (a) that the instant case presents an important question for decision by this Court, (b) that the federal question was clearly raised below, (c) that the supremacy clause requires state courts to recognize the limitations imposed by the Arbitration Act upon the power of courts to review awards, and (d) that a uniform standard of review, applicable in all states and all federal circuits, should be set forth by this Court at this time.

The Importance of This Petition

On the instant Petition for Certiorari, this Court must decide only whether to review the New Jersey courts' treatment of the arbitration award rendered in favor of Baranello against the City. It is submitted, however, that the determination of that question by this Court, which has never passed upon the standard of judicial review of the merits of an award under the Arbitration Act, will also determine whether the New Jersey courts' decisions will be permitted to operate as a signal to industry

throughout this country that commercial arbitration will henceforth be a prolonged, formal, expensive and inconclusive process which should be avoided at all cost.

Baranello's contract with the City was executed on a standard printed form promulgated by the American Institute of Architects ("A.I.A."), endorsed by the Associated General Contractors of America and used by thousands of owners and contractors nationwide. The arbitration clause printed in the contract provided for resolution of disputes pursuant to the Construction Industry Arbitration Rules of the American Arbitration Association, an organization at the forefront of dispute-resolution in this country whose credentials are universally recognized. The arbitration clause was identical to the one construed by this Court in *Moses H. Cone Memorial Hospital v. Mercury Construction Corp.*, 460 U.S. ____, 103 S.Ct. 927, 931, 74 L.Ed.2d 765, 773 (1983), in which delay claims similar to those of Baranello were declared to be arbitrable. The arbitration proceedings were administered by experienced arbitrators whose integrity and expertise in the construction industry are unchallenged.

It should be remembered that at the outset of the arbitration proceedings here at issue, the Appellate Division ruled that the arbitration clause was very broad and covered *"all* claims, disputes and other matters arising out of *or related to* the contract". *J. Baranello & Sons v. City of Paterson*, 168 N.J. Super. 502, 507, 403 A.2d. 919, 921 (App. Div. 1979), *certif. denied*, 81 N.J. 340, 407 A.2d 1214 (1979) (emphasis in original). The significance of such prior judicial finding is underscored by the following quotation from *Andros Compania Maritima, S.A. v. Marc Rich & Co.*, 579 F.2d 691, 703 (2d Cir. 1978):

> We have consistently accorded the narrowest of readings to the Arbitration Act's authorization to vacate awards "[w]here the arbitrators exceeded their powers," 9 U.S.C. § 10(d), especially where that language has been invoked in the context of arbitrators' alleged failure to correctly decide a question which all concede to have been properly submitted in the first instance.

After the arbitration award was rendered by the arbitrators and confirmed by the trial court, however, the Appellate Division in the decision now under review by this Court vacated the entire arbitration award merely because the court "cannot tell" whether the arbitrators awarded damages on certain portions of the claim which the court apparently would have denied under its own interpretation of the contract.

It is respectfully submitted that "due process" in the instant case requires reinstatement of the judgment of the trial court confirming the award. Perhaps even more important on the instant Petition for Certiorari, it is further submitted that the understandings and expectations of thousands of contractors and owners nationwide regarding the nature of arbitration should not be permitted to remain uncertain by allowing the New Jersey decision to stand unaddressed by this Court.

The Federal Statute Was Raised Below

The City's contention in Point I of its Brief that Baranello is now seeking "to amend the grounds on which they appeal to include the federal question of whether the Arbitration Act *** is applicable to this controversy", and that the federal issue "was never presented on the state level", is simply not true. Baranello obtained confirmation of the arbitration award at the trial level by a judgment which was later reversed by the Appellate Division; accordingly, Baranello's first appeal was to the Supreme Court of New Jersey. Baranello's Petition for Certification to the Supreme Court of New Jersey cited as the first of "the errors complained of" that, "The Appellate Division ignored applicable state and federal standards of review of arbitration awards ***," and further stated as follows (at pp. 6-7):

> In its review of the arbitrability of the instant dispute, the Appellate Division should also have looked to the federal law of arbitration, applicable to the City's construction contract with Baranello (a New York entity) as "a transaction involving commerce" within the meaning of section 2 of the federal Arbitration Act (9 U.S.C. §§1-14). *Moses H. Cone Memorial Hospital v. Mercury Construction Corp.*, ____ U.S.

> ____, 74 L.Ed.2d 765, 785-787 (1983); *Metro Industrial Painting Corp. v. Terminal Construction Co.*, 287 F.2d 382, 384 (2d Cir. 1961); *Sears Roebuck & Co. v. Glenwal Co.*, 325 F.Supp. 86 (S.D.N.Y. 1970), *affirmed on opinion below*, 442 F.2d 1350 (2d Cir. 1971); *Burke Public Schools Board of Education v. Shaver Partnership*, 303 N.C. 408, 279 S.E.2d 816 (1981). It has consistently been held under the federal Arbitration Act that even a "clearly erroneous" interpretation of a contract is insufficient ground to vacate an award unless the result is "completely irrational." *National Railroad Passenger Corp. v. Chesapeake and Ohio Railway Co.*, 551 F.2d 136 (7th Cir. 1977); *I/S Stavborg v. National Metal Converters, Inc.*, 500 F.2d 424 (2d Cir. 1974). ***

The federal Arbitration Act does not require that proceedings to confirm an award be commenced in federal court rather than in state court, and it should not be held that Baranello has waived its substantive rights under the federal statute merely because it cited the state statute as the procedural basis for its application in the state court for an order to show cause to obtain confirmation of the arbitration award on an expedited basis. *See Brown v. Western Railway of Alabama*, 338 U.S. 294 (1949); *Reed & Martin, Inc., v. Westinghouse Electric Corp.*, 439 F.2d 1268, 1277 (2d Cir. 1971); *Robert Lawrence Co. v. Devonshire Fabrics, Inc.*, 271 F.2d 402, 412-413 (2d Cir. 1959), *cert. granted*, 362 U.S. 909, *cert. dismissed*, 364 U.S. 801 (1960). In any event, the applicability of the federal statute was clearly raised while the case was still in the state court system, as soon as it became apparent that Baranello's federal substantive rights were not being protected. That the federal issue was squarely presented there is further demonstrated by the fact that Point IV of the City's Brief in the Supreme Court of New Jersey was entitled, "Federal Law Has No Applicability to this Case." The federal question is properly before this Court. *Pruneyard Shopping Center v. Robins*, 447 U.S. 74, 85, n. 9 (1980); *Brinkerhoff-Faris Trust & Savings Co. v. Hill*, 281 U.S. 673 (1930).

New Jersey Has Failed to Follow the Federal Standard of Review

Section 9 of the Arbitration Act, 9 U.S.C. §9, explicitly requires confirmation by a reviewing court "unless the award is vacated, modified, or corrected as prescribed in sections 10 and 11 of this title." Most courts have concluded that the strong federal policy favoring arbitration requires that Sections 10 and 11, which set forth the specific reasons for which a court may refuse to confirm an award, be applied only in exceptional circumstances.

This Court has stated, in *dicta*, that under the Arbitration Act, courts may not review an arbitrator's interpretation of either the facts or the law, even if the arbitrator misconstrued the contract language. *Commonwealth Coatings Corp. v. Continental Casualty Co.*, 393 U.S. 145, 149 (1968); *Bernhardt v. Polygraphic Co. of America*, 350 U.S. 198, 203 (1956); and *Wilko v. Swan*, 346 U.S. 427, 436 (1953).[1] Accordingly, as stated in the above quotation from Baranello's petition to the Supreme Court of New Jersey, the federal circuit courts have consistently held that the Arbitration Act restricts courts from vacating arbitration awards challenged on their merits unless the result is "completely irrational". In accord with the cases there cited are *John T. Brady & Co. v. Form-Eze Systems, Inc.*, 623 F.2d 261 (2d Cir. 1980), *cert. denied*, 449 U.S. 1062 (1980); *Swift Industries, Inc. v. Botany Industries, Inc.*, 466 F.2d 1125 (3rd Cir. 1972); *Raytheon Co. v. Rheem Manufacturing Co.*, 322 F.2d 173, 182-183 (9th Cir. 1963); *Kanmak Mills v. Society Brand Hat Co.*, 236 F.2d 240 (8th Cir. 1956).

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[1] This Court's suggestion in *Wilko v. Swan*, *supra*, that an award might be overturned where "manifest disregard" for the law were made clearly to appear, 346 U.S. at 436-437, has repeatedly given pause to courts reviewing commercial arbitration awards, and although not cited by either the City or the Appellate Division, it may be worthy of clarification by this Court. For example, in *San Martine Compania de Navigacion, S.A. v. Saguenay Terminals, Ltd.*, 293 F.2d 796 (9th Cir. 1961), the Ninth Circuit noted that "the Supreme Court's use of the words 'manifest disregard', has caused us trouble here", but concluded that manifest disregard of the law "must be something beyond and different from a mere error in the law or failure on the part of the arbitrators to understand or apply the law." *See also Saxis Steamship Co. v. Multifacs International Traders, Inc.*, 375 F.2d 577, 582 (2d Cir. 1967); *Revere Copper and Brass, Inc. v. Overseas Private Investment Corp.*, 628 F.2d 81 (D.C. Cir. 1980), *cert. denied*, 446 U.S. 983 (1980).

In the instant case, the New Jersey state courts ignored the mandate of the federal Arbitration Act, the holding of this Court in *Moses H. Cone* as to the scope of the arbitration clause in the A.I.A. contract, and the federal circuit court precedents regarding the standard of judicial review, and instead added to a long line of recent New Jersey cases which have refused to confirm arbitration awards, including *State v. State Troopers Fraternal Assn.*, 91 N.J. 464, 453 A.2d 176 (1982); *Barcon Associates, Inc. v. Tri-County Asphalt Corp.*, 86 N.J. 179, 430 A.2d 214 (1981); *In re Arbitration Between Grover and Universal Underwriters Ins. Co.*, 80 N.J. 221, 403 A.2d 448 (1979); *In re Arbitration Between Harris v. Security Ins. Group*, 140 N.J.Super. 10, 354 A.2d 704 (App. Div. 1976); *Belardinelli v. Werner Continental, Inc.*, 128 N.J.Super. 1, 318 A.2d 777 (App.Div. 1974). The dissents in these New Jersey cases demonstrate the extent of the apparent rift between the policy of New Jersey and the federal policy embodied in the Arbitration Act. For example, Justice Pashman's dissent in *Grover* began as follows:

> The majority today rules that a court may substitute its conclusion for that of an arbitrator simply because it disagrees with his decision. In so holding, it not only departs radically from existing caselaw dealing with the nature of judicial review of arbitrators' awards but, more importantly, strips commercial arbitration of its basic value.

80 N.J. at 233, 403 A.2d at 454. Similarly, Justice Clifford's dissent in *Barcon* began with the following statement:

> Presented with the opportunity to fuse the applicable law with the real world of long-standing, successful commercial practice, the Court has chosen instead to "throw a monkey wrench into the gears" of tripartite commercial arbitration.

86 N.J. at 200, 430 A.2d at 224.

At the time of the decision below, a number of states in addition to New Jersey were questioning the applicability of the federal statute in state court proceedings, *e.g.*, *Wilson & Co. v. Fremont Cake & Meal Co.*, 153 Neb. 160, 43 N.W.2d 657 (1950), *cert. denied*, 342 U.S. 812 (1951); *Standard Co. of New Orleans v. Elliott Const. Co.*, 363 So.2d 671 (La. 1978); *Pullman, Inc. v. Phoenix Steel Corp.*, 304 A.2d 334 (Del.Super. 1973). However, since the date of the decision below, this Court explicitly confirmed that the federal Arbitration Act is applicable in state court proceedings, in *Southland Corp. v. Keating*, 465 U.S. ____, 104 S.Ct. 852, 52 U.S.L.W. 4131 (1984), and summarily reversed and remanded two other arbitration cases to the Supreme Court of Georgia and the Supreme Court of Alabama, respectively, in *Local 732 v. Metro Atlanta Rapid Transit*, ____ U.S. ____, 104 S.Ct. 1263, 52 U.S.L.W. 3610 (1984), and *York International v. Alabama Oxygen Co., Inc.*, ____ U.S. ____, 104 S.Ct. 1260, 52 U.S.L.W. 3212 (1984).

We submit that where interstate commerce is involved, the State of New Jersey should not be permitted to maintain its own policy disfavoring commercial arbitration. Accordingly, this Court should at least order a remand to the Supreme Court of New Jersey similar to those in *Metro Atlanta* and *Alabama Oxygen*. In addition, however, the history of this case and of the decisions of the New Jersey courts on the subject of arbitration suggest that a clear statement of the applicable standard of review should be issued by this Court.

The City Has Not Restated the Question Presented for Review

The City has not challenged Baranello's statement of the question presented for review by this Court, namely, whether a commercial arbitration award must be vacated unless the panel has disclosed the basis of its award in sufficient detail to establish that the panel followed all technical rules of contract interpretation and all technical rules of evidence. Instead, the City argues (Point II of its Brief) that since public monies are at stake, the decision below was correct in giving the award "stricter scrutiny" and in vacating the award because the reviewing court simply

"cannot tell" whether the award includes monies which the court, on the basis of the abbreviated record filed in the confirmation proceedings, would not have awarded. Thus, the City and the decision below would shift the presumption favoring arbitration awards to a presumption disfavoring them, thereby requiring the proponent of the award to produce evidence sufficient to establish that no prescribed item of damage could possibly have been included in the award.

The arbitrators' ruling to which the City has objected, which amounted to a refusal to declare which party seemed to be prevailing on the evidence submitted up to that point in the hearings,[3] would in any event appear to fall within the category of procedural or evidentiary rulings which courts simply do not have the power to disturb under the Arbitration Act. In *American Almond Products Co. v. Consolidated Pecan Sales Co.*, 144 F.2d 448 (2d Cir. 1944), Judge Learned Hand stated as follows:

> Arbitration may or may not be a desirable substitute for trials in courts; as to that the parties must decide in each instance. But when they have adopted it, they must be content with it informalities; they may not hedge it about with those procedural

[3] Citing sections 8.3.2 and 2.2.11 of the General Conditions of the contract, the City had argued on a motion raised during one of the hearings, and later to the trial court and on appeal to the Appellate Division, that certain claims for delay were barred by a failure to have given written notice within 20 days of the discovery of the conditions. The Appellate Division vacated the award based upon its own interpretation of sections 12.1.6, 12.1.7 and 12.2.1 (reprinted in the Appendix to Baranello's Petition, pp. A-34, *et seq.*), three sections which the City had never raised and which make no reference to the arbitration process. Accordingly, Baranello was never given an opportunity to demonstrate to the court that the record before the arbitrators established that it complied with the notice requirements on which the reversal of the award was based. As observed in the City's Brief, the arbitration panel has reconsidered the evidence presented during the original hearings as directed by the decision below and awarded the contractors sums larger than those previously awarded, apparently after adding interest and attorneys' fees to the amounts of the old award. The City is challenging the new award, and Baranello is proceeding with a full reservation of rights as to the old award, and in the alternative as to the new award.

> limitations which it is precisely its purpose to avoid. They must content themselves with looser approximations to the enforcement of their rights than those that the law accords them, when they resort to its machinery.

144 F.2d at 451.

Perhaps the most serious danger of the decision below is that it runs counter to the prevailing view of the arbitration process that the arbitrators should be liberal in receiving evidence, to permit a full and fair hearing consistent with notions of due process. The prospect of lay-person arbitrators, no matter how well-intentioned, attempting to make restrictive rulings as to the admissibility of relevant evidence based upon their own understanding of the intricacies of the applicable law, is one which should not be fostered.

Even before the enactment of the first United States Arbitration Act in 1925, this Court found that equity required courts to enforce arbitration awards, holding as follows in *Burchell v. Marsh*, 58 U.S. 344, 349-350 (1855):

> Arbitrators are judges chosen by the parties to decide the matters submitted to them, finally and without appeal. As a mode of settling disputes it should receive every encouragement from courts of equity. If the award is within the submission, and contains the honest decision of the arbitrators, after a full and fair hearing of the parties, a court of equity will not set it aside for error either in law or fact. A contrary course would be a substitution of the judgment of the Chancellor in place of the judges chosen by the parties, and would make an award the commencement, not the end, of litigation.***

Since the award in this case was rendered for a lump sum, there is no way to tell whether any damages were in fact awarded for the delays which the court said had been waived, and therefore the award should have been sustained. In *Burchell v. Marsh*, *supra*, this Court upheld a lump-sum award over an objection similar to that made in the instant case, stating as follows:

> It has been argued, that because the arbitrators received evidence of the slanderous language used by Cross, that, therefore, they included in their award damages for his slanders, for which his principals would be liable; and that, therefore, they had taken into consideration matters not contained in the submission. But the answer to this allegation is, that the record shows no admission or proof that the arbitrators allowed any damages for the slanders of Cross. *** Every presumption is in favor of the validity of the award. If it had stated an account, by which it appeared that the arbitrators had made a specific allowance of damages for the slanders of Cross, it would have been annulled to that extent at least, as beyond the submission. But it cannot be inferred that the arbitrators went beyond the submission, merely because they may have admitted illegal evidence about the subject matter of it.

58 U.S. at 350-351.

In sum, it is respectfully submitted that a uniform standard of review of commercial arbitration awards, applicable in all states and all federal circuits, should be enforced by this Court in order to give effect to the strong federal policy favoring arbitration addressed by this Court in *Moses H. Cone* and *Southland*. The forum selection principles set out in those decisions will be of little avail to litigants unless arbitration awards, once rendered, can be enforced in the courts.

CONCLUSION

Baranello's Petition for Certiorari should be granted.

Dated: Washington, D.C.
May 31, 1984

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